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ECONOMIC RESEARCH
AND ANALYSIS

**Ben Johnson
Associates, Inc**

July 6, 1992

FCC MAIL BRANCH

Office of the Secretary
Federal Communications Commission
1919 M Street, N.W.
Washington, D.C. 20554

Gentlemen:

Please accept these comments submitted on behalf of
the Indiana Office of Utility Consumer Counselor and
the Pennsylvania Office of Consumer Advocate in CC
Docket No. 92-77 regarding 0+ dialing. The original
and nine (9) copies are enclosed.

Sincerely,



Ben Johnson, Ph.D.
President

BJ/mw

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**Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554**

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Federal Communications Commission
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FCC MAIL BRANCH

In the Matter of)

CC Docket No. 92-77

Billed Party Preference)

for O+ InterLATA Calls)

**COMMENTS OF THE
INDIANA OFFICE OF UTILITY CONSUMER COUNSELOR
AND THE
PENNSYLVANIA OFFICE OF CONSUMER ADVOCATE**

The Indiana Office of Utility Consumer Counselor (Indiana) and The Pennsylvania Office of Consumer Advocate (Pennsylvania) respectfully submit these comments in response to the Notice of Proposed Rulemaking ("NPRM") adopted by the Federal Communications Commission ("FCC") on April 9, 1992.

I. INTRODUCTION

The FCC initiated this rulemaking proceeding to consider the merits of an automated "billed party preference" method of routing O+ interLATA traffic from payphones and other locations. As described in the Notice, under a billed party preference system, O+ interLATA calls placed from payphones (and possibly other locations) would be routed to the operator service provider (OSP) which is preselected by the party being billed for the call. Thus, a O+ collect call would be routed to the OSP preselected by the called party, while a O+ call billed to a third party would be routed to the OSP preselected by the third party. Currently, such calls are routed to an OSP that has been preselected by the payphone owner or by the owner of the premises on which the phone is located.

The FCC has tentatively concluded that billed party preference routing of all O+ calls is in the public interest and seeks comment in this proceeding on the costs, benefits, and implementation of such a system.

Indiana and Pennsylvania applaud and strongly endorse the FCC's proposal to initiate a billed party preference system for all O+ interLATA calls. As described more fully below, the current system of routing such traffic does not comport with the public interest, due to market failures caused by such factors as monopoly power, barriers to entry, and lack of perfect information. Our comments will address the following topics: (1) the historical background; (2) the economic theory of competition and the conditions required thereby; (3) the ways in which the current system fails to meet these requirements and thus fails to protect the public interest; (4) the ways a billed

party preference system can promote effective competition and thereby protect the public interest; (5) alternative methods of implementation and their implications for the competitive process and long-term customer satisfaction; and (6) the scope of the billed party preference system.

II. THE HISTORICAL BACKGROUND

Prior to 1989, Bell Operating Companies (BOCs) routed all 0+ interLATA payphone traffic to AT&T. On January 29, 1988, the Department of Justice filed a motion claiming this practice to be in violation of the equal access provisions of the Modification of Final Judgement (MFJ).

In response to the Department of Justice motion, the BOCs and various interexchange carriers (IXCs) presented proposed equal access plans for BOC payphones. On October 14, 1988, the Court ruled that "a system which permits the billed party to select the interexchange carrier of his choice simply by dialing 0+ most perfectly comports with the language and purposes of the decree." [*United States v. Western Electric Co., Inc.*, 698 F. Supp. 348, 367 (D.D.C. 1988).]

At that time, however, equal access was as abstract an ideal as a balanced federal budget. The information technology required for its implementation was not available. The Line Identification Data Base (LIDB) necessary for implementation of what later became known as "billed party preference" had not yet been completed. And so, the Court ordered the BOCs to implement an interim system of "equal access" by which the owners of the BOC payphone premises could presubscribe the originating 0+ interLATA traffic to a specific OSP.

Although relegating this choice to the middleman rather than the end user deprived "equal access" of consumer sovereignty, the Court hastened to add that it "expects the Regional Companies will continue expeditiously to perfect the LIDB system which, when placed into service, will permit full compliance with the decree." Moreover, it left the door open to revisit this issue "at a future date to determine what further arrangements and orders, if any, are necessary," but suggested that action by the FCC might render future Court action moot. [*United States v. Western Electric Co., Inc.*, 698 F. Supp. 248, 367 (D.D.C. 1988).]

On December 23, 1988, the Court also ordered GTE to implement a presubscription program for its payphones. At the same time, however, the Court restated its earlier position that "this solution does not fully satisfy the requirements of the GTE decree." The Court "instructed" GTE "to work towards implementation of technology that will allow the actual customer to select the interexchange carrier of his choice using 0+ dialing." [*United State v. GTE Corp.*, C.A. No. 83-1298, slip op. (D.D.C. Dec. 23, 1988) at 4-5.] If there were any doubt regarding the Court's intent, it was removed. In fact, the phrase "allow the actual customer to select the interexchange carrier of his choice using 0+ dialing" succinctly defines billed party preference.

BOC and GTE payphones have subsequently been presubscribed to an OSP chosen by the owner of the premises on which such payphones are located. Other public phones, including those in hotels, motels, and other aggregator locations, are currently

presubscribed to an OSP chosen either by the payphone provider or by the premises owner. The OSPs generally offer commissions on 0+ calls made from phones pre-subscribed to them.

As a result, the caller who wants to use a carrier other than the presubscribed one cannot use the more convenient and familiar 0+ dialing. Instead, the customer must dial an additional code of five digits (10XXX), seven digits (950-XXXX) or eleven digits (1-800-XXX-XXXX). But even that may not suffice. In some instances, premises owners or payphone providers have blocked access code dialing, thereby preventing callers from reaching their OSP of choice, and forcing them to use the OSP selected by the person controlling the phone.

In 1988 the Common Carrier Bureau found access code blocking to be an unjust and unreasonable practice in violation of Section 201 (b) of the Communications Act, except as necessary to prevent fraud, and required that the identity of the pre-subscribed OSP be available to callers using phones under presubscription contracts. Shortly thereafter, the FCC initiated a proceeding to consider general rules regarding access code blocking, consumer information, and other related areas. [Policies and Rules Concerning Operator Service Providers, CC Docket No. 90-313, Notice of Proposed Rulemaking, 5 FCC Rcd 120 (1990); Report and Order, 6 FCC Rcd 2744 (1991).]

In October 1990, Congress enacted the Telephone Operator Consumer Services Improvement Act (TOCSIA), which directed the FCC to require within a "reasonable time": (1) the unblocking of equal access 10XXX codes at all aggregator locations; and/or (2) establishment by all OSPs of an 800 or 950 access number. [Codified at 47 U.S.C. § 226.]

In CC Docket No. 91-35, the FCC adopted rules requiring payphone providers to unblock equal access (10XXX) codes by March 1992 and other aggregators to unblock those codes in various time frames over a period of approximately six years. The FCC also required OSPs to provide 950 or 1-800 access (also effective March 1992). [Policies and Rules Concerning Operator Service Access and Pay Telephone Compensation, CC Docket No. 91-35, Report and Order and Further Notice of Proposed Rulemaking, 6 FCC Rcd 4736 (1991).]

Thus, with some exceptions, consumers should currently be able to select an OSP of their choice when using a payphone by dialing a 10XXX access code prior to dialing zero plus the number being called. However, customers using phones at hotels, motels, and other aggregator locations may still be prevented from selecting the OSP of their choice, if the owners of the telephones at such locations continue to block 10XXX access. Even where access to the preferred OSP is not blocked, consumers may not be provided sufficient information to "call around" the preselected OSP—or else they may be simply too confused to do so. Moreover, because of the difficulty of policing the thousands of them that operate throughout the country, some private paystation providers continue to block callers from dialing 10XXX, thereby forcing these callers to use whatever OSP the paystation provider has selected.

Why O+ Dialing Is Important

Some parties have claimed that since equal access allows the caller to dial carrier access codes, billed-party preference is a mere luxury. However, whether dialed at public telephones, residences, or businesses, access codes have proved themselves unpopular with consumers. Even aside from the various exceptions and violations of the rules mandating availability of 10XXX access, the simple fact is that this method of access has never gained full public acceptance. Hence, it makes little sense to advance it as a valid solution to the problems with the existing, temporary, system whereby the OSP is selected by someone other than the customer. Callers do not want to be burdened with the dialing of additional digits; they want to reach their chosen OSP without being forced to use an inconvenient and unpopular dialing pattern.

Under the current system of equal access, dialing a O+ credit card call is already a finger exercise in twenty-five movements (the "O," the ten digits of the called number, and the fourteen digits of cards in the current AT&T or BOC format). While one could ask what's the harm of a mere five digits more, the fact is that callers continue to resist dialing them.

Where equal access is not available, and callers must use "950" and "800" access codes to reach their chosen carriers, the dialing demands are even more onerous—seven or eleven more digits added to the twenty-five normally used for a credit card call. Since these codes, lengthy as they are, work in all end offices, some carriers instruct their customers to use them everywhere, in order to promote the use of a single code. The carrier in such instances manipulates the caller into dialing thirty-six digits where "only" thirty would have been necessary. While this "solution" may be acceptable to the carrier, and it avoids some of the worst abuses, it is not an optimal solution from the consumer's perspective.

Of course, the caller is not always the billed party. On a collect call, the billed party is the other party. For parties frequently receiving collect calls, routing to their preferred carrier would guarantee billing at agreed to rates, but many callers who reverse the charges will not know the preferred carrier of the called and billed party. Thus, even if they know the carrier's access code and are willing to dial the additional digits, they may find it impossible to choose the carrier preferred by the customer they are calling. [According to AT&T, 46 percent of collect calls are placed to the caller's own home or office, but this leaves 54 percent which are not. See AT&T's Comments on Bell Atlantic's Petition on or about May 26, 1989.]

Many O+ calls are misrouted. National Data Corporation handles over 100,000 Sprint calls per day with its operators, most of which arrive through O+ dialing. Sprint claims that 30 to 40 percent of these calls are requests to bill calls to BOC or AT&T calling cards, which National Data Corporation presently cannot validate.

The Ameritech Operating companies presently handle their own O+ calls in three states. Upon receiving such calls, the operator instructs the caller to hang up and dial "O+" or "OO-." If the carrier associated with the originating line does not serve O+ calls, the customer generally hears a recording upon reaching the POP, which usually instructs him to dial 10288 + O plus the number. Despite these explicit

instructions, Ameritech in these three states receives 14,000 calls per day from callers who have failed to reach their desired carrier. On a national basis, this extrapolates to some five million mis-routed calls per month. [See Petition of the Ameritech Companies for Amendment of Part 69 of the Rules to Enable Exchange Access "Dial O" Services To Be Provided by Local Exchange Carriers, No. RM-6113, filed August 7, 1987, pp. 1-3.]

The original intent of presubscription was to minimize or eliminate lengthy access codes and still allow the customer free choice. This condition has simply not been achieved with respect to calls placed from any location other than the customer's home or business. For calls placed from paystations, hotels, hospitals, and similar locations, consumers today still do not have effective control over the service provider; nor can they effectively control the amount they pay for the service they are forced to accept. Even to the limited degree consumer sovereignty has been achieved, people are forced to use cumbersome, time-consuming and unpopular dialing procedures.

The Nature of Current Consumer Complaints

As it turns out, the evolution of the operator services industry during recent years has for many customers made an operator service call—especially from a public telephone—a complex, tedious, and exasperating experience. Consumers using the familiar and popular O+ dialing pattern are often confused and frustrated by the following:

- their lack of knowledge of the actual rates charged until the telephone bill from a presubscribed service is received (a month or two months later);
- low quality service at unexpectedly high rates;
- the division of responsibilities between the local and long-distance telephone companies;
- their misunderstanding or lack of information as to which carrier will be handling a call charged to a particular calling card;
- their inability to use one, consumer-selected OSP for all their calls;
- their inability to make all operator-assisted calls on a O+ basis;
- being required to remember and use access codes, as well as to know when to use them;
- the necessity and inconvenience of determining when to dial an access number for their own OSP, as well as having to perform the extra dialing; and
- having an OSP refuse to route the call in the manner expected (call blocking).

These continuing consumer complaints point directly to significant market failures. Prices are being set at noncompetitive levels, often for substandard service. Moreover, some of the dominant carriers now may be in a position to use consumers' confusion as a wedge to prevent the emergence of effective competition.

Consumers with imperfect knowledge are being forced to incur substantial information costs as well as transactions costs that would be eliminated by an effective system of billed party preference. Worst of all, consumer sovereignty, the centerpiece of free markets, has been replaced by middleman and con-man sovereignty.

In addition to protecting captive consumers from overcharges, the FCC's proposed billed party preference ruling also promises to bring needed improvements in customer convenience, competitive behavior, O+ calling rates, and the structure of both the long-distance and the operator service provider (OSP) industries.

For various reasons discussed below, effective competition has failed to develop under the current O+ dialing system; and, consequently, the public interest has generally been neither protected nor promoted. In order to explain why this failure has occurred, we will first outline the market conditions necessary to effective competition and then compare them with the realities of the current interstate and interLATA O+ markets. We shall consider only those competitive criteria relevant to this context.

III. THE CONDITIONS FOR COMPETITION

From the buyer's perspective, a primary requisite is knowledge of the market. Consumers who are unaware of the choices available to them are incapable of functioning as efficient allocators. From the perspective of micro-economic theory, decision rules describe the decisions people make about things like consumption rates and choice of suppliers. Outcomes from these decision rules summarize the information people use to make those decisions. From a given and well-known set of rules of the game, such as the O+ rules prevailing for some thirty years, the consumer made reliable and predictable choices. Service quality was uniformly maintained by the Bell System, working in partnership with the independent telephone companies. Prices were uniformly maintained within each state and within the entire nationwide interstate market. Thus, each time consumers placed O+ calls, they knew what quality they would receive and approximately what price they would pay.

More recently, however, the market has changed drastically. Consumers cannot be expected to make efficient choices under the current system. The rules have changed in such a way that full information is simply not available. Unless the OSP is one the customer is familiar with, that customer will not be able to anticipate either the quality of service to be supplied or the price to be charged. This system totally violates the requirements of complete information and precludes customers from effectively functioning on the basis of rational expectations.

Another extremely important initial consideration underlies any analysis of production and allocation. Both buyers and sellers must view price as a given. All participants in the market must behave as if market prices are unaffected by their own decisions regarding how much they should purchase or produce. As we will explain in

detail below, with the current system for O+ traffic, this criterion is not met. On a national scale, AT&T clearly dominates the market and can greatly influence the nationwide level of O+ prices. And, on a local scale, OSPs that have been selected to receive all O+ calls from particular paystations and hotel phones can determine the level of prices paid by consumers placing O+ calls from those locations. This type of control over pricing by sellers is prima facie evidence of market failure.

We will return to these points later. Meanwhile, since we know the numbers of consumers of telephone services to be numerous, we will begin by focusing on the production or supply side of the ideal market. Usually, four conditions are considered sufficient to assure that firms will behave as "price takers," or idealized competitors.

First, no one firm can have a dominant share of the market. If a firm engages in price leadership, dominant firm pricing, or price discrimination, its behavior is inconsistent with competitive behavior.

Second, the products of the supplying firms must be generally uniform (from the perspective of the buyers in the market). If consumers view the product or service as unique, the firm will not need to behave as a "price taker."

Third, the number of supplying firms must be large enough so that the total amount supplied to the market cannot be restricted. It always is in the interest of suppliers to limit the total amount supplied to the market, because they can then charge a higher price and earn greater returns (economic profits) than under the conditions of competition.

Fourth, firms must be free to enter and exit the industry. If any firm decides to produce the service, no substantial legal, financial, or other barriers must stand in its way. Patents or trademarks (such as brand names) and other legal barriers also can preclude competition. A firm otherwise qualified for entry faces not only its own inertia but the difficulty of competing with an established firm and brand. Advertising start-up costs may be high, and the new firm may face short-term losses. If greatness of scale is necessary for earning reasonable returns, the costs of entry may be so large as to discourage potential entrants.

Only if every one of these consumer and supplier conditions is satisfied can we be confident that competition will characterize the market.

Derivatives

A pair of theoretical stances in current economics are also relevant to this discussion. First, the theory of contestable markets is an extension of the theory of competitive markets. Contestability theory relies on the disciplinary effect of potential competition. If, for example, a telephone company could enter a new market quickly with low sunk costs, the threat of entry would be sufficient to cause competitive pricing behavior among the existing firms.

Contestability theory nonetheless sharply contrasts with one of the traditional conditions of perfect competition. Instead of requiring many firms, contestability theory says that the number of actual competitors should have no effect on prices. While the theory is interesting, the conditions required by the theory (effortless, costless,

instantaneous entry and exit by firms) are never met in practice. As a result, real world outcomes, including those with the deregulated airlines industry, suggest that potential competition is not an adequate substitute for actual competition.

A second notion closely related to idealized competition is the Coase Theorem. It states that under conditions of perfect competition and minimal information and transactions costs, the allocation of clearly defined property rights generating or being affected by externalities leaves the allocation of resources (and output mix) unchanged. The ownership of the property rights is irrelevant: so long as the ownership is clearly established, perfect information exists, and transaction costs are minimal, economic efficiency can be achieved.

Telephone services presently are supplied under public regulation by a mix of IXC's, LEC's, and premises owners. Since all these suppliers are involved, property rights are difficult to define. In this production form, the virtual inseparability of sometimes conflicting claims to property rights can only be resolved by an "outside arbitrator," perhaps a state public utility commission, the FCC, or both. Thus, the clarity of property rights depends upon the decisions of the public regulators—most importantly the FCC.

In the present instance, wherein O+ service is produced in part by IXC's, LEC's, paystation owners, and premises owners, the definition of property rights is definitely muddled. Moreover, under the present system, the conditions of perfect information and minimal transactions costs are grossly violated.

IV. MARKET FAILURES IN O+ CALLING SERVICES

Clearly, the current O+ market fails to meet any of the requirements for effective competition.

Buyers' Imperfect Knowledge

Consumer sovereignty is largely absent in the current system due to the lack of information available to end users. Although the FCC and many state regulatory commissions have required OSPs to identify themselves to end users (through tent cards and announcements), they are not required to provide any information concerning rates, except upon request. Accordingly, callers routinely purchase O+ service—for which they will not be billed until weeks later—without being aware of the rates they will be charged. This contrasts sharply with the typical market transaction (e.g., at a grocery store), where the price is clearly shown to the customer before the purchase, or at least is paid at the time of the transaction (thereby allowing the customer to change his mind before it is too late).

The limited rules that have been imposed on the O+ market are simply not sufficient to correct the problems. Most customers are unfamiliar with the intricacies of the long-distance market, do not know the names and rates of every OSP, and thus do not know whether or not they will be overcharged if they place a O+ call. And since calls are of widely varying durations and distances, a charge that is 50% or more in

excess of the lowest competitive rate may be paid without a murmur by the unwitting customer.

Due to the utter absence of perfect information, gross inefficiencies and market imperfections persist. Customers continue to be routinely overcharged without realizing the extent of the problem or reacting to it.

Under extreme circumstances—for example, when a customer is charged \$40 for a phone call that should have cost less than \$9—the barrier of insufficient knowledge may be penetrated, and the customer may react. Even at that point, however, the reaction is unlikely to be consistent with an effectively competitive market. Instead of becoming an expert on the intricacies of the O+ market and on the precise rates charged by each OSP at every location in the country, the average consumer will probably retreat to the security of the largest carrier. Thus, the dominance of the largest carrier will be enhanced, the market will become less competitive, and the potential for economic efficiency will be reduced even further.

Moreover, some OSPs use separate billing agents for their billing and collection activities. A customer may receive a bill from an entity that did not actually provide the operator service, and the bill may not identify the OSP or provide a customer service number that the customer can call with questions or complaints. Customers who have been grossly overcharged by an OSP may continue to use that firm because they are never informed of its name (only the billing agent's); and thus even if they read the fine print on the payphone or tent card, they may not realize they are dealing with the same firm that has abused them in the past.

Customer confusion also arises under the current system from the lack of ubiquitous equal access and the lack of consistent requirements for the unblocking of 10XXX codes where equal access is available. For instance, a customer using a paystation can presumably now reach his/her carrier of choice by dialing an access code; however, that customer cannot use the access code in a nonequal access area or from a hotel that blocks such codes. Moreover, since many aggregators—along with most end users—presubscribe to AT&T, customers will often have O+ calls routed to their carrier of choice by coincidence without dialing an access code.

Accordingly, a lethargy factor also reduces the effectiveness of the market mechanisms. Customers may accept occasional overcharges in return for the convenience of O+ dialing, since most of their calls are carried by AT&T and the price is acceptable (although not necessarily at a competitive minimum).

Nonhomogeneity of Service

The present presubscription system also violates another condition for effective competition: homogeneity of the product or service. Consumers have complained that O+ service is sometimes of inferior quality. This seemingly random variation in quality adds to their frustration, since the problem is not apparent until the call is completed, and any attempt to hang up and select an alternative provider will be highly inconvenient and costly.

Poor service in itself would not be a problem under competitive conditions. The consumer would boycott the firms providing inconsistent or inferior service, and losses by the supplier would force the carrier to exit the industry or upgrade quality. In the present situation, however, the consumer doesn't know whether the problem lies with the OSP, or the LEC, or the paystation provider. And, since the problem can be highly localized and seemingly random, there is little that rational consumers can do in order to assure themselves of uniformly high quality.

Limited Number of Sellers (Often Just One)

Under the current system, aggregators (airports, hotels, motels, etc.) and premises owners (food stores, service stations, etc.) exclusively select one carrier for O+ traffic. Being court-ordered, this amounts to an exclusive franchise granted to a single seller—as if an airport were to grant an exclusive franchise to one car rental agency or one food services firm.

Given the preference of the caller for O+ dialing, and the fact that the premises owner is not paying the bills or experiencing the service quality, the situation is ripe for abuse. In many instances, this exclusive franchise is granted for reasons which are not consistent with the public interest—such as maximizing commission payments. The most pernicious effects of this exclusive franchising system are visible in airports. A traveler between flights hasn't time to leave the airport to seek an alternative OSP. Even if time allowed, the excursion could be inconvenient and costly.

A traveler lodged in a hotel or motel faces a similar though less extreme dilemma. The inconvenience and loss of time might be less than for the air traveler, but they could still be significant. It is unreasonable to expect consumers to travel from one retail establishment to another seeking their preferred carrier in order to place calls on a O+ basis without fear of poor service or excessive rates.

Depending upon the nature of the aggregator, the consumer is "captive" in various degrees—a hostage of the enterprise. Since the telephone and the selected OSP are site-specific, many of the conditions of a local monopoly are present.

It is commonplace in economics to claim that no producer, not even one enjoying a pure monopoly, can escape the influence of consumer demand. At prices which are too high, it is said, the monopolist will lose customers. Also, at high prices, if the monopolist is making high profits, the magnetism of these profits to potential competitors is very strong. So we might say that no producer, no seller ever has complete, absolute "monopoly power" as long as the market is "contestable."

In the present instance, however, it is apparent that substantial barriers to effective competition exist. Obviously, hostage consumers at the airport have little choice but to use the airport's phones. Of course, they still have the option of dialing thirty to thirty-six digits in order to reach a trusted OSP. But few consumers seem willing to do so. As long as the great majority of all travelers refuse to use elaborate access codes and insist on using O+ dialing patterns, the market failures can be expected to continue.

Consumer resistance to using laborious alternatives makes the price elasticity of demand relatively low in such circumstances. Therefore, phone rates can be set at levels that are relatively high on the steeply-sloping demand curve. Such prices provide monopoly profits for unscrupulous OSPs (which charge excessive rates) and some aggregators and premises owners (which receive excessive commissions). Moreover, these monopoly profits persist because the exclusiveness of the franchise prevents even the threat of entry. In most instances, the market is not only noncompetitive, it is largely incontestable. Under the present system the aggregators and premises owners are paid commissions by the selected carrier. Such commissions amount to a major component of the price for calls. The commissions are not uniform. They are designed to sway the aggregator or premises owner into selecting the particular negotiating carrier.

The premises owner will be biased toward the high-commission sales, sometimes without regard to the quality of the services. Most travelers are not even aware of such commission overrides and do not realize that the premises owner has a reason to prefer one carrier over another—not necessarily the same reason the end user would have.

InterLATA carriers such as AT&T have been paying average commission rates of about 15% on the average revenue per completed call of \$2.40, or 36 cents per completed call. AT&T also has been paying the cost of "direct selling" to premises owners, maintaining a dedicated sales force for major accounts and utilizing many general business salespeople on a "part-time" basis. Moreover, a substantial advertising and promotion budget is targeted to premises owners.

If we assume a 10 percent "cost of selling" (24 cents per call), the cost of wooing premises owners amounts to about 60 cents. From a national perspective, when multiplied by tens of millions of calls each year, this is a substantial sum. Bear in mind that this 60 cents is expended on millions of calls for a largely superfluous function (selecting a presubscribed OSP) which involves little more than a few minutes of decision making on the part of the premise owner or aggregator.

Furthermore, many carriers (excluding AT&T) inflate presubscription costs through "premises owner surcharges." These incremental per-call interLATA charges are often 50 cents or \$1.00 and are billed to the end user as if they were part of the cost of the call. In reality, these surcharges are remitted entirely to the premises owner.

Since it is easy to pass along such "marketing costs" to a hostage consumer, the commissions can be very high. Under such a system of bribery the aggregator or premises owner may be more concerned with the commission rather than the quality of the services of the OSP, or the fairness of the prices charged.

The demand curve of captive consumers is unique. In competitive markets the supplier would face an aggregate demand curve for phone services. In the captive marketplace consumer demand is comprised only of the select few who—for the time-being—have been preselected to use the only available OSP. Their consumer interests can be safely ignored, unless retaliation is forthcoming once the travelers receive the bill and remember where they placed the call.

Many years ago, economist John Kenneth Galbraith made claim for an economic phenomenon he called the dependence effect. By means of advertising, promotion, and salesmanship, wrote Galbraith, the producers create many of the wants they seek to satisfy. The shape of the automobile, for most people, will be what the automobile majors decree the current shape to be. Hence, there is in the American economy something more like producer sovereignty. However problematic Galbraith's claim might be when it is applied to other markets, clearly the current system of O+ presubscription has granted sovereignty to the OSP preselected by the aggregator. The violation of the fundamental principle of consumer sovereignty is no way doubtful in this particular context.

Conclusions

The widespread dissatisfaction with O+ dialing has resulted from the failure of the current system to focus on the needs and demands of the end users who pay for the services of the OSPs. As noted in the NPRM, the present system rewards OSPs that are able to attract the largest number of paystation and other aggregator locations—typically, the OSPs that can pay the highest commissions. Where transient uses of telephones are involved, the present system gives OSPs little, if any, incentive to provide high-quality service at “competitive” rates.

In fact, for the smaller OSPs, the real “customer” is the paystation provider, hotel, or motel, not the end users who actually pay for their services. The OSP tries to attract business by paying high commissions to the premises owner, rather than offering lower prices and/or higher quality service to end users. Likewise, the premise owner has strong incentives to encourage or force customers to use the services of the OSP to whom that owner has presubscribed, in order to increase the amount of traffic carried by the OSP and boost its own commissions. Furthermore, the owner has some incentive to accept or even encourage the OSP to charge high prices for its services, if commissions are based on a percentage of billed toll usage.

Thus, the incentives that normally protect the public interest in an effectively competitive market are generally absent in the O+ toll market. In a competitive market, rival firms are pressured to operate efficiently, offer quality service, and charge competitive rates in order attract market share and encourage growth in demand. In the O+ market, OSP providers serving transient consumers generally do not face those pressures.

Another defect in the current system is that even when the calling customer is able to reach his/her carrier of choice, that carrier may not be the choice of the customer to whom the call is billed (e.g., the call recipient for collect calls, or the third party for third party billing). This flaw reflects another departure from the workings of more typical competitive markets, in which the consumer who pays for the product or service can choose the provider.

The current system produces both winners and losers. One significant winner appears to be AT&T, which benefits in the commission system from its historical dominance of the long-distance market. As noted in the NPRM, AT&T's dominant

share of the 1+ market makes it an attractive OSP for aggregators, who know that many customers will choose to use AT&T and thereby ensure them high commissions. Due to the amount of traffic routed to it, AT&T can remit a lower percentage commission than smaller OSPs while still paying higher commissions overall.

Another group of winners under the present system are unscrupulous OSPs which impose excessive charges on transient consumers and which often offer inferior service. Despite regulatory reforms at both the federal and state levels designed to protect the public from such firms, many remain in operation, and more continue to enter the market. These firms clearly have the opportunity to enjoy supranormal profits, given their high rates relative to the low cost of providing operator services.

Finally, motels, hotels, convenience stores, airports, and other businesses that control prime locations for outgoing long distance calls are clear winners under the current system, since they receive monopoly rents in the form of commissions on the OSP traffic originating from their locations. These businesses incur little if any cost to maintain public telephones at their locations; thus, the commissions they receive are nearly pure profit.

The number of losers under the current system far outweigh the number of winners. They include customers who are faced with grossly excessive rates charged by unscrupulous OSPs which they neither selected (knowingly) nor had any desire to do business with; customers of AT&T and other major carriers who pay excessive rates for operator-assisted calls that greatly exceed the direct costs of such calls; and MCI, Sprint, and smaller legitimate OSPs which find it difficult to compete effectively with AT&T, given its dominant market position, and which must try to overcome the poor reputation that the OSP industry has been saddled with by their shady counterparts.

Admittedly, much of the "winning" and "losing" in this situation simply involves transfers of wealth from one category of society (e.g., end use customers) to another category (e.g., unscrupulous OSPs and greedy premise owners). However, there are also some very substantial loss to society from inefficiency and unnecessary costs. They include the added costs of millions of uncompleted calls when customers place O+ calls to carriers they do not want to use, and millions of hours of wasted time expended by live operators, hotel desk clerks, and end users due to the inconsistent, confusing, and risky nature of the current system. While each customer inquiry, uncompleted call, and frustrating dispute may involve only a minute or two, the cumulative total for the nation is very substantial indeed. This enormous waste of society's resources can be avoided only by a fundamental change in the system.

V. VIRTUES OF BILLED PARTY PREFERENCE

A ubiquitous billed party preference system would remove many of the underlying causes of the market imperfections discussed above. Most importantly, it would shift the OSPs' focus to the end users who pay for their service. To compete successfully, an OSP would have to offer a combination of services and prices that satisfy the end users in its target market. The competitive process in the O+ market would thus be focused on customer satisfaction in all of its dimensions, including price, ubiquity of

service, technological improvements and value-added features (e.g., voice mail, store and forward messages), and quality in all its dimensions (e.g., transmission clarity, call set-up time, etc.).

Particularly if implemented ubiquitously, billed party preference would also eliminate much of the confusion and frustration that exists under the current system. Consumers would not have to know when it was necessary to dial an access code to reach their carrier of choice; they would be assured that simply by dialing 0+, the call would be carried by the preselected OSP of the billed party. Additionally, consumers would not be confronted with bills from carriers that they did not choose and whose service they did not want. They would receive bills only from OSPs of their choosing, and could select the OSP that offered the desired combination of price and service.

A billed party preference system would also have the advantage of eliminating from the 0+ market the unscrupulous OSPs that charge exorbitant rates and are able to remain in business only because of their presence at limited locations serving the transient public. If all consumers were able to preselect the 0+ carriers of their choice, the market niche for unscrupulous OSPs will undoubtedly disappear. Customers are likely to select 0+ carriers which offer competitive rates, an attractive array of service, and/or a name and reputation that the customer trusts.

VI. IMPLEMENTATION

Indiana and Pennsylvania recommend that the FCC implement universal billed party preference in four stages. These stages are defined so as to make clear the ultimate intent of the FCC in the rule-making process as well as to minimize the long-term cost of implementation.

Stage I: The Initial Ruling

First, Indiana and Pennsylvania recommend that the Commission immediately issue an order mandating universal billed party preference within a prescribed time frame. It is the proper regulatory responsibility of the Commission to provide unambiguous rules for the industry. This would give the FCC leadership in a case which otherwise might be returned to the Court.

Stage II: Transitional But Universal 10XXX, 950 or 1-800 Access

Indiana and Pennsylvania recommend that the Commission immediately mandate all OSPs to provide a complete advertising and public information program making clear to consumers that callers can—through appropriate procedures—reach their OSP of choice by dialing extra digits.

Stage III: Expedited Technological Improvements

Universal billed party preference cannot be implemented prior to the complete deployment of CSS7 and LIDB. Since these systems will eventually be deployed irrespective of whether billed party preference is implemented, the Commission should

encourage an acceleration in the deployment of this technology, as long as the costs are not excessive.

Stage IV: Rules For The Routing of Calls

1. An LIDB query would not be necessary on calls made with IXC calling cards. When an IXC calling card is used, Indiana recommends that the LECs either identify the OSP at the OSS itself by reading the first six digits on the card or query the issuing IXC's data base for routing.

2. Under LIDB, Indiana and Pennsylvania recommend, LECs would enter the LIDB system in which they have designated a primary and secondary choice for each telephone line. The LIDB would contain a secondary OSP choice for calls originating in areas where the primary OSP was unavailable, thus enabling customers to select a small, regional OSP as their primary OSP without losing the ability to originate O+ calls in areas their primary OSP does not serve.

3. Billed party preference also could be designed to permit a separate OSP selection for international calls.

4. The LIDB system information would be used for carrier identification purposes on O+ interLATA collect and third party calls, as well as calls billed to LEC calling cards, which would continue to be either line-number based or in the Revenue Accounting Office (RAO) format. (A line-number based calling card has a fourteen-digit account number, with the first ten digits being the subscriber's telephone number. An RAO card also has fourteen digits, but its ten-digit billing number replaces the ten-digit phone number.)

5. Despite these many possible changes, some things would remain the same. The routing of calls via an access code or via 1+ would not be altered under billed party preference. Access code calls would be routed directly to the IXC associated with the dialed access code, and the 1+ calls would continue to be routed to the carrier presubscribed to the originating line. Moreover, OO- calls (where O is dialed twice) would continue to be routed to the operator service of the IXC presubscribed to the originating line.

VII. SCOPE OF BILLED PARTY PREFERENCE

Indiana and Pennsylvania believe that the maximum benefits from a billed party preference system would be obtained by making the system ubiquitous for all O+ calling. That is, billed party preference should be available from all paystations, motels, hotels, and other aggregator locations nationwide and from all private business and residence phones. If technically feasible at a reasonable cost, we believe that the system should be provided in both equal access and nonequal access serving areas.

Ubiquitous implementation would avoid the confusion that might result if billed party preference were mandated only from certain types of telephones (e.g., payphones). Limited implementation would tend to dilute the benefits of the system,

particularly that of allowing customers to know that dialing only 0+ will ensure the routing of their call to the preselected OSP of the billed party.

Respectfully submitted

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